

The Free Market

"If you don't create a free market, a black market will emerge"



NEWSLETTER OF THE LITHUANIAN FREE MARKET INSTITUTE - www.freema.org/Newsletter/index.phtml

NEWS

LFMI proposes solutions for health care reform

On 19 February 2003 in Vilnius, the Lithuanian Free Market Institute will hold a seminar "Measures for Reforming Health Care System: Financing or Solutions?" The aim of the seminar is to increase public awareness about the need to reform the financing of health care system and spring forward a new approach and ready solutions. At the event, LFMI will present a conceptual framework for the health care system reform in Lithuania that would allow quality medical treatment and transparent financing. The seminar will also address the problems of compensation for pharmaceuticals, private health insurance, and the principles of distribution of mandatory health insurance fund.

The seminar is organised within the framework of LFMI's project "Creating Financially Viable Health Care System in Lithuania" which aims at promoting an effective health care system in Lithuania, in line with the free market principles. The developed package of policy proposals on health care reform will be finalised after the seminar and disseminated widely among decision making institutions, the medical community, media, and the general public.

LFMI's course on freedom continues

In February 2003, LFMI will start delivering a semester-long university course *Capitalism and Freedom* for a third year, which is aimed to instil in students self-conscious liberal thinking through the study and internalization of sound social and economic ideas. By giving this course, LFMI seeks to develop a tradition of teaching freedom as a subject that requires profound public understanding. It is tailored for second-year students of law, economics, political science, sociology, philosophy, journalism, and others. This year the course will be delivered at Vilnius University and the International School of Management.

LFMI's course on freedom was launched in 2001, when LFMI became a winner of the Sir John Templeton Foundation's International Freedom Project, directed by the Atlas Economic Research Foundation. This project aimed to encourage and support studies on freedom in the universities of many countries. An international jury of judges selected fourteen applications, among which was LFMI's application for the course. Other winners were universities from Italy, Spain, Australia, Philippines, Montenegro, Serbia, Russia, Turkey, France, Nigeria, and Guatemala.

For a detailed description of the course, please visit our home page at <http://www.freema.org/Projects/Course.phtml>.

A survey on the ethics of civil servants and politicians

In November 2002, LFMI and the international organisation *Transparency International* conducted a survey which was aimed at eliciting the attitudes of people in Lithuania to the ethics of civil servants and politicians.

The survey showed that nearly half of Lithuanian people have negative opinion about the ethics of civil servants and politicians. Forty-one percent of the respondents evaluated their ethics as unsatisfactory; 9.5 percent reported that state officers did not follow the norms of ethics at all. Forty-five percent of those polled voiced a satisfactory opinion about the ethics of state officials.

According to the survey, people are most disappointed with the level of ethics in the parliament; officers in ministries were evaluated as the most ethical. People in Lithuania believe that

civil servants and politicians break the ethics because they want to attain personal gain, lack responsibility, feel total impunity, and have opportunities to abuse the official power. The majority of the respondents, 43 percent, think that state officials lobby for group interests and 32 percent believe they protect personal interests.

The main source of information about unethical behaviour of officials is mass media. Slightly less than a half of the survey participants learned about unethical behaviour from personal experience and one-third, from relatives and friends. A total majority of people in Lithuania support the idea that stricter rules of conduct should be imposed on civil servants even outside their service.

Asked if they had heard about the codes of ethics of civil servants and politicians being drafted, 70 percent of the respondents reported negative answers. Sixty-four percent believe that the said codes will be adopted albeit not at one fell swoop.

LFMI presented the results of this survey to Parliament Chairman Arturas Paulauskas and the parliamentary commission of anti-corruption as well as at a press conference.

LFMI submits recommendations on the EU future

In the autumn of 2002, LFMI completed and disseminated a study *Debate on the Future of Europe: a View from Lithuania* which presents the principles of, and recommendations for, reforming the EU and its institutions, dividing competencies among the EU and member-states, and drawing the citizens into decision-making process of the EU.

The study developed by LFMI is the first comprehensive collection of analysis-based recommendations that was prepared in Lithuania with a view to joining the debate on the future of EU.

The study provides a short presentation of the on-going debate about the future of Europe and its major issues. It also presents a description of EU institutions, their functions, the fundamental principles and methods of the EU, and the explanation of major terms. Most of the study was devoted to formulating specific recommendations for the development of EU activities in order to ensure better conditions to implement the goals of the EU and to establish democratic and effective methods of activities of the EU after the enlargement.

The main conclusion of this study is that the EU currently operates under the rules which allow for a good balance between legitimacy and effectiveness. The main challenge for the EU and, in particular, its member states is to observe in its daily activities the main principles which are set forth in its Treaty and to take the current rules of decision making seriously.

The study was prepared in English and Lithuanian and submitted to institutions of Lithuania and the EU as well as the organisers of the Convention on EU Future. The study was developed within the framework of LFMI's project on the future of Europe, supported by European Commission Delegation in Lithuania PHARE Small Grants Programme and the Swedish Embassy.

FEATURE

"The Free Market" offers a presentation by LFMI's Vice-president Ruta Vainiene delivered to an international conference "Tax Competition and Competitiveness" held by the Lithuanian Free Market Institute in co-operation with the Heritage Foundation, U.S.A., and the Friedrich Naumann Foundation, Germany, on December 5-6 2002.

Lessons to Lithuania. Challenges to the European Union

Ruta Vainiene, Vice President, LFMI

On board a plane once I found an interesting article in *The Financial Times*. Even though I have not saved it physically, which is a pity, I remember its contents perfectly well. It was a short article about a pressure by international institutions on low-tax-rate countries (offshore countries) to raise taxes and to stop the game of harmful competition. The article quoted the response of the head of government of Jersey - one of the offshore countries - essentially implying: why should we raise taxes if with low tax rates we are able to collect the funds sufficient for funding the government. I was amazed at the straightforwardness and simplicity of the reply. You have to agree that one can hardly imagine the head of our or a neighbouring state uttering such firm and indisputable words.

We are mainly used to quite a different type of rhetoric followed by particular steps in the area of tax reform. "In line with the European Union directive requirements". "This contradicts the practice in the EU". "This is the way most European Union Member States do". For several recent years such taxation arguments have become familiar to our ears. No one even really attempts to dispute the argument of integration into the European Union. Trying to adapt and not to stand out, this is true even in those areas where no formal requirements

exist. I do understand why. This is convenient and safe for those who suggest and those who implement tax reforms since they claim: it's not my idea, so responsibility is not mine either. As I see it, Lithuanian politicians would certainly agree on harmonising all the taxes, there would be less trouble and thinking for them.

Fortunately not all European Union Member States are of this view, therefore direct taxes are still an issue of competition. It is common knowledge that attempts to harmonise all the taxes have failed, and so far a compromise solution - the Code of Conduct binding in the field of direct taxation seems to be considered as a satisfactory level of regulation. Nevertheless this does not mean that alignment is not an item of discussion agendas. There were, are and will be attempts to have uniform taxes in the European Union, or at least drive towards such uniformity. The rhetoric used referring to tax competition is more or less as follows (my quotation is taken from an information publication, a booklet on EU taxation system that is a perfect reflection of prevailing views): Tax competition. Decisions about investment, business activities, jobs and earnings are sensitive to differences in national tax regimes and social welfare systems. With increasing mobility and differentials in tax bases, business can identify the components on which they are taxed (taxable bases) and shop around to find the country where tax is lowest. Such competition between Member States puts downward pressure on the level of tax and contributions which may be damaging if it is not regulated, as it undermines the fairness and overall efficiency of tax system. You see. I will come back to these statements in my presentation later.

The conference has extensively debated in search for answers to questions: do we want to have tax competition, can harmonisation contribute in any way, in other words, which is better - having the same or different tax systems.

I would first of all like to say a few words about a political aspect of tax competition in order to exhaust this matter and to get to exceptionally economic issues. So, a political aspect of tax competition is especially closely linked with democracy, as tax competition is first and foremost the result of democracy in a free world. People elect a government that sets certain taxes. It is due to democracy functioning in the predominant majority of world countries that people have "what they elect". Tax competition and democracy are two interacting factors. For democracy to continue to be a reality, people need to have a real and not a nominal possibility of choice. In case with the help of universal harmonisation of taxes lower level governments were deprived of an opportunity to exercise their influence in such a significant area - there is no doubt about it - as taxes, the public's incentives to "participate in democracy" would be considerably diminished. Democracy itself would be diminished. As much as I know, the flag of democracy is still flying in all the countries that have raised it, which suggests that a fully-fledged democracy needs to be characterised by the authority of the elected power to change things, as well as the understanding that people get that their ballots matter. Otherwise, why go and vote for a government that does not decide about key matters, and how to choose from all equally same things?

I would like to generalise now by saying that tax competition is the result of democracy and its safeguard in the world. Because it is evident that if one (higher, more distant) government encroaches on the power of the other (lower, local), people will lose interest in the limited lower government, which will lead to undermining democracy. The latter sentence does not imply that I am against limiting government as a mechanism of coercion. A self-willed government is effectively limited by competition, in order to be fully-fledged it must have a multifaceted extensive possibility of decision-making.

The modern world experiences tax competition, which is a result of a political as well as economic choice. An opportunity granted by politics to tax competition has given an individual, beside other freedoms, the freedom of economic choice, while tax competition has clarified human choices, their preferences. What are the preferences in terms of taxes?

Well, there is no simple and agreed answer as to what animal a tax is. Is it a paid service of a state, or just a tool of redistribution? Taxes combine both in all the countries, for that reason when dealing with human choices, both cases should be considered.

In the instances where taxes are payments for services provided by a state, acquisition of a certain function performed by the state, or an unusual way of buying from a particular supplier in a market, each rationally thinking individual is keen on getting a service of the highest possible quality at the lowest possible price. A rational individual acts according to this pattern, according to my observation, unless one is a character of jokes about “nauveaurish”. That means to say that, with other circumstances being the same, an individual always makes a choice out of the same quality services based on price. An individual always wishes to buy the cheapest desired service, and the fact that the service is provided by the state does in no way affect an essential criterion for choice. A person is ready to pay a higher price only in case he/she is buying a service of a higher quality or has no choice at all. My conclusion comes as a question to the audience: is there a better way than competition to promote higher quality services and lower prices? Competition and competition alone has the power of realistic consumer protection. It is for this particular reason that the European Union is so actively safeguarding competition between individual entities. Let's draw a parallel with services provided by the state then: modern tax harmonisation that resembles cartel arrangements should also be prohibited. And as totally different rules are applied to taxes, consistency for the sake of declared values seems to be lacking.

In another approach to taxation, an individual is considered as a source paying money and never getting anything from a state in return. In other words, taxes are an instrument of redistribution. In that case an individual's need to wish taxes as low as possible is evident. Great as a sense of solidarity might be, sympathy for the weak can never eliminate an individual's wish to sympathise and contribute in a personal and personified manner, in addition, he/she has to wish to do so in certain amounts and reduce a compulsory contribution. What a situation might help him/her pay too high a price for solidarity? The question brings me back to competition.

Thus, the presence of one's need to pay low taxes does not call for proof supported by special studies or experiments. Life itself as well as human choices made in their everyday lives confirm one's need for low taxes. The proof lies in the popularity of offshore countries, the size of capital flows going there, and the depth and width of shadow economy, therefore the conclusion is that a human being is just human, and his/her wish to live better is still there, it has not disappeared.

At this point I would like to return to my quotation about the harm of tax competition in the European Union, which argues that competition between Member States exerts pressure on the level of taxation. The European Union realises that tax competition is a precondition of tax reduction. A conclusion suggests itself that tax harmonisation is aimed at protection from such a pressure. A glance at EU directives brings about immediate realisation that they set a minimum tax rate. What they really do is watchfully protect governments from too low a level of taxation. This motif underpins the endeavour of harmonising taxes in Europe. Crows will not pick crows' (government's) eyes, as a proverb goes.

Is there another way of ensuring lower taxes? Can tax harmonisation perform the said function? Referring to harmonisation, I do not refer to the one undertaken by the European Union by setting floor tax rules, I refer to the one when ceiling tax rules are developed, while a government's greed cannot overstep the set ceiling. First, such a solution cannot be expected in several coming decades, second, it would limit the possibilities of those who wish to see higher taxes and better government services, and third, where is the margin of the ceiling that must not be exceeded? What if the margin is set at a relatively high level and if everybody hangs onto it claiming that it is justifiable. Lithuanian municipalities serve as good examples of the latter. They enjoy the right to establish some taxes for their budget tax revenues within certain maximum limits drawn. The result is easy to guess - the municipalities do not doubt about imposing the highest tax rates.

One would not dare contest the truth that the lower the taxes the lower the need to have them different. Tax competition is not beneficial in itself. It is a possibility of having low taxes that is beneficial. Should such an opportunity be offered by equal tax rates, need for different tax rates would be phased out.

The presence of different taxes is encouraged by a strong economic-cultural, historic and geographic factor, thus numerous reasons, numerous externalities or developments have decided that income taxes prevail in some countries' budget revenues, consumption taxes are predominant in others, while some rely on natural resource taxes. For different reasons some countries have chosen one or another scheme of taxation, which has taken root in that particular state. Nonetheless, what suits and functions in one country may be a failure in another if an attempt is made to copy and implement the latter's scheme there.

This rule is also applicable to a tax structure, i.e. what taxes are imposed, and what their rates are. Since countries differ in income levels, a tax burden on different country taxpayers' shoulders is different. We, Lithuanian population, have

experienced that disproportion ourselves when excise taxes have been and are still being raised to the European level in recent years. In view of fundamental differences in income, Lithuanian people overpay for financing the needs covered by revenues from excise taxes. And as the imposition of excise taxes rests on the need to finance mitigation of negative externalities, the disproportion in taxation may lead to numerous negative consequences. Tax evasion grows, and labour gets more encouragement to migrate where it can have better possibilities of earning and "carrying the tax burden". A vicious circle of interdependent chains and developments is activated: the budget collects too little and inefficiently, possibility to finance externalities reduces, attractiveness of a state to both labour and capital reduces, possibility to implement the state budget diminishes. Generally speaking, the countries that undertake to carry an unacceptable tax burden are destined to take a slow but straight road to becoming a province and are deprived of a chance to head to prosperity.

So far each country has survived by having found ways of efficient and effective taxation for itself, as tax analyst Alan Reynolds noted at the conference on taxes organised by the LFMI in as early as 1997, by having found the least painful way to skin a cat. There is no way one can deny the existence of fundamental country differences (mentality, traditions, income, a geographic and historical position), neither can one deny or change the phenomenon of taxation, so what is left to do is to tolerate different taxes and consequently tax competition in hope of having efficient taxation. Any resistance to this reality, imagining things rather than facing the reality makes harmonisation either inefficient or simply impossible.

All the efforts to align taxes meet huge technical challenges in both making decisions on tax uniformity and implementing them.

All the previous conclusions about the existence of competition, let's call them lessons, are addressed to the European Union willing to harmonise and to Lithuania willing to obey. My conclusion, which will come at a later stage of my presentation, will also be addressed to both Lithuania and the European Union, and I would like to call them challenges to harmonisation. (In fact, I might give my contribution a different title "Lessons of competition. Challenges to harmonisation. To Lithuania and the European Union").

I have already noted that competition is an existent fact. Beside tax competition we might talk about a certain tax segment harmonised in a certain area. The challenge is posed, what are the responses?

It would be only too naïve to think that if indirect taxes were harmonised in the European Union, competition would be eradicated. Of course, not. First, it would penetrate into other taxes. Second, competition between a taxed economy and an untaxed (shadow) economy would be more severe. Third and most important, the area of competition is the whole world rather than Europe or the European Union only. A closed and uniform Europe could be a discussion item when the world was divided and closed by what may be called physical walls, when no physical, technological, informational possibilities for moving in space and time existed. There are different attempts

made to localise and tax e-commerce and trade in derivative securities. But all the attempts are hopelessly lagging behind progress in the field of globalisation. Technologies, in this instance, serve for the purpose of realistic globalisation, and maybe, for the better, and maybe, for the worse, impede surrender and obedience to harmonisation.

Choosing from between fight against progress and world-wide movement, on the one hand, and acceptance and realisation that the more diversified choices there are in the internal space, the smaller is the need to look for them outside, on the other. This is an important challenge to harmonisation. And now, the more progress is made in uniformity or synchronisation of taxation, the greater will the pressure to choose either - or... Either stay in the area or withdraw as the area of choice narrows. The European Union vitally needs competition in its area for the Union to be able to compete globally in trade, investment, i.e. economic activity area.

Listening to my presentation, you might get an impression (or you must have already got an impression) that I am definitely against harmonisation. I am trying to prove that competition is a smart guy, and that harmonisation is faced with lots of challenges. So now I have come to the point when I want to destroy the possibly wrong impression because I have nothing against harmonisation, and I want to explain against what particular harmonisation I am not against.

When Friedrich A. von Hayek argues about social order, he mentions two patterns of social order "an imposed order" and "a grown order", or "coerced" (sometimes even military) and spontaneous, or *taxis* and *kosmos*. And even though Hayek tells about these orders in a broad legal context, these two patterns of order or the way they become prevalent can be successfully applied to tax law.

In reality all the talking about a different or the same tax environment moves to another field. We are not talking about an end, all the results will be, most probably, accepted in the end if they are obtained by way of natural and non-coercive development. The same applies to taxes too, absolutely the same taxes would be acceptable if each country found, introduced and retained them in its own way. Such an instance of spontaneous harmonisation is fully possible, realistic and real. Let's glimpse at the tax systems of different states, all of them have followed a similar evolution. The method must have been that of copying when some countries would take on board other countries' systems. If they proved to be appropriate there, they would be retained, if they did not, they would be rejected. For that reason all the countries have income tax, and do not tax windows or beards. This does not mean that the similarity of taxes has been decided upon and commanded, what I suggest is that the process was spontaneous. It has been dictated by need (whether the need is reasonable is another story) rather than the declaration of a uniform tax regime. There is just one general argument against spontaneous tax harmonisation - a shortcoming typical of all the methods - spontaneous tax harmonisation is implemented by a government, but with only a small degree of certainty that it will not decide to expand "spontaneously". A spontaneous development and competition of governments provides more choice for people and by doing so limits government arbitrariness.

May the harmonisation undertaken by the European Union be called spontaneous, or should it be labelled "coercive"? Evidence of spontaneousness is in accession, which is voluntary, hence the result of choice. However, the key is the internal policy of the European Union and its attempt to raise an issue of harmonisation. As I mentioned at the very beginning when I dwelt on the aims of harmonisation, the single (unified) Europe implies, beside other things, that it is the same all over. Non-acceptance of differences, wish to have in birds of a feather that flock together - this is an attribute of a coercive order. And there comes one more challenge to the European Union - how much can the declared economic values as well as political rights be realistically ensured. The future of Europe will depend on how this challenge is met. Larger doses of spontaneous order, which in no ways does not mean 'no order', would be in the interests of the Union itself.

ACTIVITIES

October – December 2002

Company law

In order to avoid the abuse of rights by small shareholders, LFMI's policy analysts evaluated positively a draft amendment to the Law on Joint-Stock Companies, initiated by the Ministry of Economy. The proposed amendment stipulates that the minority of shareholders shall consist of shareholders holding no less than 10 percent of the total number of votes in the company. On the one hand, all shareholders should be granted equal rights; on the other, a limit should be set for the number of shareholders needed in order to influence the decision-making in the company, so that the decisions necessary for the management and activities of the company were passed efficiently.

LFMI also analysed a draft law on sole proprietorships and submitted comments to the Ministry of Economy. LFMI proposed to allow for one person to own several sole proprietorships and to restructure sole proprietorships by way of both mergers and divisions.

LFMI's policy analysts also studied draft amendments to the Enterprise Bankruptcy Law and pointed out questionable draft provisions regarding the liability of the head of company and the owners, the right of the interested persons to cover the court and administration expenses, and the court's refusal to initiate bankruptcy proceedings. However, the parliamentary committees turned down LFMI's proposals.

Deregulation

Licensing. In the past years, a number of changes to the legal framework of licensing were implemented. Yet, major problems remained unsolved. In light of this, LFMI's policy analysts carried a comprehensive overview of specific features of licensing regulation and procedures that build preconditions for corruption and abuse of official power and submitted recommendations to government institutions regarding the principles of licensing reform. LFMI's policy analysts also participated in a working group on licensing regulation and submitted proposals on the licensing principles that would

allow ensuring consistency in reforming the existing licensing rules and procedures as well as safeguarding against eclectic and unjustified decisions.

Building and land purchase. Implementing a project "Real Estate Registration and Mortgage Systems in Lithuania", LFMI hosted, Nov. 14, a seminar "Is It Easy to Become a Real Estate Owner?" Recently on a rise, the real estate market further highlighted the drawbacks of the system of real estate registration. Despite the fact that the real estate register ranks among the technically best-maintained registers in Lithuania, the buyers and sellers of real estate still need to go through lengthy and costly real estate registration procedures in order to buy, sell and (or) mortgage real estate. The seminar addressed possible solutions for improving the system of real estate registration, which would facilitate the sale and purchase of real estate and would help the banks to shorten the time of granting loans and the people and companies – to acquire real estate more easily. LFMI will continue its activities in this area and will further propose essential changes in the system of registers.

Customs. LFMI's policy analysts have repeatedly called for the simplification of import procedures and have invited relevant government authorities to scrap customs-related business restrictions. As of January 2003, a new procedure of import of telecommunications equipment came into force in Lithuania, no longer requiring a license for importing telecommunications equipment that meets the EU requirements. Also, administrative taxes have been abolished, and conformity documents issued in the EU countries are now recognised in Lithuania. The new procedure has significantly facilitated the import of mobile telephones, car security systems, analogous and digital telephones, faxes, modems and other items.

Education

LFMI and the Knowledge Economy Forum organised a conference 'Higher Education in Lithuania: Diagnosis and Prognosis,' which was held in Vilnius Nov. 5. The goal this event was to generate a discussion on Lithuania's higher education policy, which would contribute to the creation of an effective system of higher education, improvement of the quality of higher education in line with technological advances and market demand, and development of high-quality student-orientated study courses with the demand on the market. LFMI presented a framework of the proposed reform in higher education system.

In its resolution regarding granting state loans to students, the Government included LFMI's proposals and set out the conditions of loan repayment that allow paying off a loan from funds of any economic entity and not necessarily in cases when the said-provision is included in a labour contract. Moreover, a provision was rejected allowing the writing-off of a loan for those students who have worked in a state or municipality institution for five years. The said resolution also indicates that loan quotas for higher education establishments will be fixed on the basis of the number of students paying for their tuition rather than the total number of students at those establishments.

At the request of the Open Society Fund Lithuania (OSF), LFMI has carried out an analysis to evaluate whether a draft law on education will help or hamper non-public education. At

a meeting at the Parliament, Nov. 18, the Education Studies Centre of OSF presented its experimental assessment of the draft law on education, incorporating the conclusions by LFMI.

EU integration

LFMI has conducted a study “Debate on the Future of Europe: a View from Lithuania,” which presents an analysis of the issues currently debated in the EU and gives recommendations on how to respond to major challenges that the EU is facing before accepting new members. The study is the first exhaustive collection of analysis-based recommendations in Lithuania, presented in response to the invitation to join the discussion on the future of Europe. The study appears in Lithuanian and English. It has been presented to Lithuania’s government institutions and the EU institutions as well as the organisers of the Convention on the Future of Europe.

Foreign trade

In fulfilment of its obligations to the World Trade Organisation, the Government has changed or lifted import duties from some goods brought into Lithuania. New import duties became effective as of December 16, 2002. Seeking to harmonise competition conditions for oil producers and importers, the conventional import duty tariff on engine and gearbox oils was reduced from 10 percent to the 3.7 percent rate applied in the EU. LFMI’s policy analysts, involved in the activities of the Tariff and Non-tariff Barrier Elimination Commission, have regularly opposed the introduction of new import duties and advocated the abolishment of the existing ones.

Health care

LFMI has continued participating in the debates on draft national pharmaceuticals policy at the parliamentary Committee on Health Affairs. After LFMI submitted its policy recommendations, the draft document was improved significantly, although still failing to provide for the reform of pharmaceuticals policy.

While debating draft amendments to the Law on Health Insurance, the parliamentary Committee on Health Affairs took into account two principal recommendations by LFMI regarding the laying down of the obligation by the State Patients’ Funds to pay fines for delayed payments and the size of contribution for persons insured by the state. The Committee rejected many other recommendations, e.g., to narrow the list of state-insured persons and the services to be compensated for. Also, the Committee did not turn down a new provision stipulating that “the manufacturer’s prices used for calculating the base price of a pharmaceutical to be compensated for shall be lower or not higher than 5 percent than the lowest price of the corresponding pharmaceutical produced in the EU countries.” LFMI believes that a possible ambiguous interpretation of this provision will have negative consequences for the consumers of pharmaceuticals.

LFMI also took part in a working group under the President of the Republic of Lithuania that was set up to develop strategic regulations for pharmaceutical activities and control thereof which developed a draft of the final document. At a meeting with the President, the working group presented the key elements of the reform which are vital for ensuring transparent compensation for pharmaceuticals. LFMI’s Vice-president

Guoda Steponaviciene underlined that pharmaceutical activities would lack transparency for as long as there existed a list of medicines entitled to compensation. MPs sitting on the working group also acknowledged that the general and strengthening position of the group was to replace the list of pharmaceuticals entitled to compensation with the list of diseases entitled to compensation. To eliminate the list of compensated pharmaceuticals, as a step towards greater transparency and competition in the pharmaceutical system, was also proposed by the State Control.

LFMI organised a workshop Oct. 2 to discuss major problems in health system as identified by LFMI when analysing the health care system. The workshop was attended by 23 health professionals, among them physicians, insurers, pharmacists and analysts. It was aimed at identifying the problematic elements of a viable health model as well as formulating proposals for their elimination.

Housing policy

After the Government opposed the introduction of contractual savings system (the so-called “Bausparkassen”) and after the Parliament started debating a draft law regulating this model, LFMI submitted to the parliament its comments on the expediency of the said piece of legislation. LFMI’s policy analysts also took part in the debates of the draft law at the parliamentary Committee on Economics and pointed out the negative effects of its introduction.

When drafting a law on mortgage bonds and mortgage lending, a working group included LFMI’s proposals and eliminated the restrictions on credit beneficiaries and the utilisation of the credit. Currently debated by the Parliament, the draft law will regulate a new housing financing instrument, a mortgage lending system. On Nov. 14 LFMI hosted a seminar “Is It Easy to Become a Real Estate Owner?” which highlighted once again the shortcomings of the bill: it is laid down that mortgage-lending services will be provided and mortgage bonds will be issued by credit institutions only. In principle welcoming this model of housing financing, LFMI proposed the parliament to soften the said restrictions and thus create more favourable conditions for introducing a more flexible and locally-suited model of mortgage lending in Lithuania (as compared to the contractual savings system).

The results of LFMI’s survey on Lithuanian households became an important element of the draft National Housing Strategy, currently under preparation by the Ministry of Environment, providing exhaustive information to those putting forward housing policy solutions.

Whilst implementing a project on the assessment of housing support programmes, LFMI, in co-operation with the Urban Institute, U.S.A., analysed the existing policies of housing support. Two interim presentations of the results have been held at the Ministry of Environment and LFMI’s proposals, formulated in a project material, have been included into the draft National Housing Strategy.

Information technologies

LFMI’s Vice-president Guoda Steponaviciene is a member of a working group under the parliamentary Committee on the Development of Information Society, which is to draft a new version of the Law on Electronic Signature. The working group

presently holds discussions on whether a state centre for the certification of electronic signature should be established. LFMI maintains that the provision of the effectual Law should be preserved, according to which market participants who will need electronic signature certification will create such services themselves.

The majority of proposals by LFMI have been included into the concept of e-government adopted by the Government Dec. 31. Their essence is to maintain the principle of decentralisation and commercialisation of e-government projects, which are embedded in a draft of the document. The team that drafted the concept failed to avoid a number of unnecessary and populist provisions and attached too great importance to institutional supervision. The latter might create conditions for centralising the management and implementation of e-government projects.

As the Parliament started debating draft amendments to the Law on Copyright and Related Rights, LFMI analysed provisions regulating the author's remuneration. LFMI argued that taxation of blank medium and equipment used for reproduction, embedded in the draft document, is inappropriate. LFMI proposed other models for regulating author's remuneration based on the traditional interpretation of ownership rights and on modern technologies which would ensure protection of these rights.

Knowledge economy and telecommunications

LFMI's Vice-president Guoda Steponaviciene presented to the Knowledge Society Council under the President of Lithuania LFMI's position regarding problems of the regulation of the telecommunications market encountered in the implementation of the new Law on Telecommunications. Ms. Steponaviciene pointed out that a major problem in this regard is not in the timely development of secondary legislation but rather in ensuring the appropriate quality of the legislation adopted. The main hurdles in the liberalisation of the telecommunications market are the instability of legal environment and failure to meet the principle of minimum regulation (especially in drafting secondary legislation).

Guoda Steponaviciene has also been participating in a working group to draw up a conceptual framework of the law on electronic communications. With regard to the funding of Communications Regulatory Authority (CRA), LFMI submitted a proposal that CRA should be financed from fees paid by economic entities for its traditionally provided services and from the budget for the performance of the market supervision functions entrusted to it by the new Law on Telecommunications (similar to the funding of the Competition Council). As a result of debates on this issue, a compromise was reached and the wording was adopted, under which CRA is funded from two sources as it is provided for in the new law (without specifying which functions are financed from which sources). LFMI also put forward a proposal on the key issue raised in the said conceptual framework – the efficient frequency allocation. LFMI's proposal to allow the holders of frequency bands to re-rent them out on the market was rejected. In LFMI's opinion, the conceptual framework developed by the working group is formal, leaving all the essential and contentious issues open, which will eventually result in their resurfacing in the further drafting of the law.

Therefore, LFMI's vice-president abstained from voting on the final document.

LFMI presented its comments regarding the World Bank report on the overall business environment, higher education system and innovation when the World Bank mission was visiting Lithuania to assess the possibilities for knowledge economy capabilities in the country. After the mission developed a new report, LFMI submitted its comments identifying the essential flaws in the proposals made by the World Bank. LFMI criticised a weighty focus on institutions (rather than their functions), the inadequacy of measures proposed for higher education reform (the proposed measures would fail to make a real difference as the system's problems lie in the principles of its financing), and a sketchy assessment of the impact of tax reform on the activities of high-tech companies, without assessing the ineffectiveness of the state's initiatives and its detrimental impact on competition and motivation of market participants.

NGO legislation

LFMI has analysed a draft of a new version of the Law on Lobbying Activities and submitted its comments to the Parliament. Under the draft law, virtually any kind of activity including the expression of opinion on draft legislation would become lobbying. LFMI's policy analysts stated that such amendments constitute an unjustified restriction of human rights, endanger democracy and do not conform to the globally accepted understanding of lobbying, while translating such provisions into practice would be impossible. According to LFMI, a new version of the Law on Lobbying Activities is unnecessary and might cause a chaos in the regulation of lobbying activities and law making. LFMI presented its position at a preliminary sitting of the parliamentary Committee on Legal Affairs. Representatives of LFMI also attended a press conference held by Non-Governmental Organisations Information and Support Centre, during which the NGOs' representatives voiced concern over the said draft law debated by the parliament. As a result of these efforts, certain changes were introduced in the draft law, yet, the major shortcomings were not eliminated.

Pension system reform

The Parliament has eventually enacted the Law on Pension System Reform. Welcoming the adopted model of the reform, LFMI's policy analysts pointed out that the Parliament could have set a considerably larger share of social insurance contribution, at least 5 percent, which will be diverted from the government-run social insurance system to private personal accounts. The adopted law provides that only 2.5 percent of the contribution will be transferred for private accumulation.

Public administration

Ethics of civil servants: In a press conference, Nov. 26, LFMI presented the results of a survey aimed at finding out the opinion of people in Lithuania about the ethics of civil servants and politicians. The survey was carried out in co-operation with the international anti-corruption organisation 'Transparency International.' On Nov. 27 LFMI's President Ugnius Trumpa and Policy Analyst Aneta Piasecka presented the results of the survey to Chairman of the Parliament Arturas Paulauskas and the parliamentary Anti-corruption Commission.

Legislation: A specialist commission headed by LFMI's Policy Analyst Remigijus Simasius developed a draft plan of legislature improvement which is aimed at stopping chaotic law-making and ensuring better co-ordination of legislative initiatives of different institutions.

Social policy

After the Government approved a draft law on monetary social support and submitted it to the Parliament, LFMI revised its policy recommendations (formulated for the initial draft of the law) and submitted them to the Parliament. LFMI thinks that the government-approved draft law regulates the rendering of monetary support more clearly but fails to remedy the major shortcoming of social welfare system in Lithuania – the linking of social benefits to several criteria and the variety of the forms of support.

LFMI's policy analysts also underlined that even though a conceptual framework of social insurance against unemployment, drawn up by the Ministry of Social Affairs and Labour, attempts to adapt social insurance to the principles of insurance, this is a costly process that fails to change the taxing nature of social insurance.

Tax policy

LFMI, in co-operation with the Heritage Foundation and the Friedrich Naumann Foundation, held a two-day international conference "Tax Competition and Competitiveness. Ten Years of Experience and Challenges for the Future" Dec. 5-6, Vilnius. The conference was held under the courtesy of His Excellency Valdas Adamkus, President of the Republic of Lithuania. The conference addressed the specific features of tax systems in the Baltic States and Russia and their impact on business, investment and economic growth, the role of tax planning in seeking competitiveness and the policy of the said countries regarding "tax havens." Also, a presentation of the EU tax legislation and the practice of tax harmonisation and tax competition was made. The event gathered around 250 participants including parliament members from the Baltic States and Russia, high-ranking government officials, ministry executives, policy analysts from the Baltic States, Russia and the EU, and representatives of international institutions and the academia.

The working group on taxation at the Sunrise Commission, headed by LFMI's Vice-president Ruta Vainiene, continued its work and discussed the following issues and drafts of legal documents: the procedure of taxation of income in kind, a draft law on inheritance tax, draft amendments to the law on profit tax, and the problems of leasing companies pointed out by the association of leasing companies. The Ministry of Finance backed the majority of proposals by the working group.

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If you don't create a free market, a black market will emerge

The founders of LFMI are – Prof. Kęstutis Glaveckas, Nijolė Žambaitė, Dainius Pupkevičius, Petras Auštrevičius, Elena Leontjeva and Darius Mockus.

LFMI pursues its mission by conducting research on key economic policy issues, developing conceptual reform packages, submitting policy recommendations at the legislative and executive levels, drafting and evaluating legislation, and launching public campaigns. LFMI's activities also include sociological surveys, publications, conferences, workshops, and lectures.

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